Borrowers Beware

Use a lender you know and trust. An unscrupulous lender may try to pull one of these common scams:

Equity Stripping

This is a practice where loans are made to consumers without regard to the borrower's ability to pay. For instance, an unscrupulous lender may encourage you to overstate your income on the loan application in order to get the loan approved, knowing you will not have the income to cover the monthly payments. You may also be encouraged to borrow more than you need so you will have extra spending money, knowing you won't have this money available when it is time to make payments. As soon as you default on the loan, the lender will foreclose, taking your home and the equity in it.

Loan Flipping

A lender convinces you to refinance your home. You agree and make a few payments on the new loan. The lender then approaches you offering a bigger loan for something such as a "dream vacation." When you accept the new offer, the lender refinances the original loan, lending additional money. In doing so, you are charged high points and fees and an increased interest rate for each refinancing. You'll also have to pay any prepayment penalties each time. The result is more debt over a longer period of time.

"Home Improvement Loan Scams"

A contractor offers to do some work on your home, saying he can also arrange the financing through a lender. Once you agree, the contractor begins work. The lender then appears with papers to sign. He may rush you into signing a document before you have time to read it, or the contractor may threaten to stop working until the papers are signed. You sign, only later realizing you've just agreed to a home equity loan with high rates, points and fees. Additionally, the contractor now has no interest in finishing the job, since he has already gotten paid by the lender.

Signing Over the Deed

You can't pay your mortgage and face foreclosure. A "lender" contacts you, offering help. First, the lender requires you deed the property to him, claiming this is a temporary safety measure to prevent foreclosure. Once the lender has the deed, he owns your property. He can borrow against it or sell it to someone else. The lender can treat you as a tenant, using the mortgage payments as rent. Once you default on the payments, the lender can evict you from your own home.

Tips

SHOP AROUND

Once you have determined which type of loan is best for you, check with several lenders, compare terms, rates and conditions. Is the application fee refundable if you don't qualify or decide not to accept the loan? What is the APR (annual percentage rate)? Is it fixed or adjustable? Are there caps on the interest rate? Does the loan require a balloon payment at the end of the term? What are the points? Are there closing costs? Is mortgage or credit insurance required? Is there a prepayment penalty? Will you need a home appraisal to see if you qualify?

THE LENDER

When you have chosen a lender that can meet your initial requirements, try to negotiate. Perhaps the lender could lower the APR, or remove a term you don't like. Make sure to ask the lender for a blank copy of the forms you will get at closing. Be certain you can afford the loan; if you can't, you could lose your home.

THE DEAL

Before closing, ask for an explanation of anything you don't understand. Never sign a loan agreement if the terms differ from what you were originally told or if there are blanks to be filled in later by the lender. Finally, make sure you get a copy of all the documents you sign before you leave the lender.

THE CLOSING

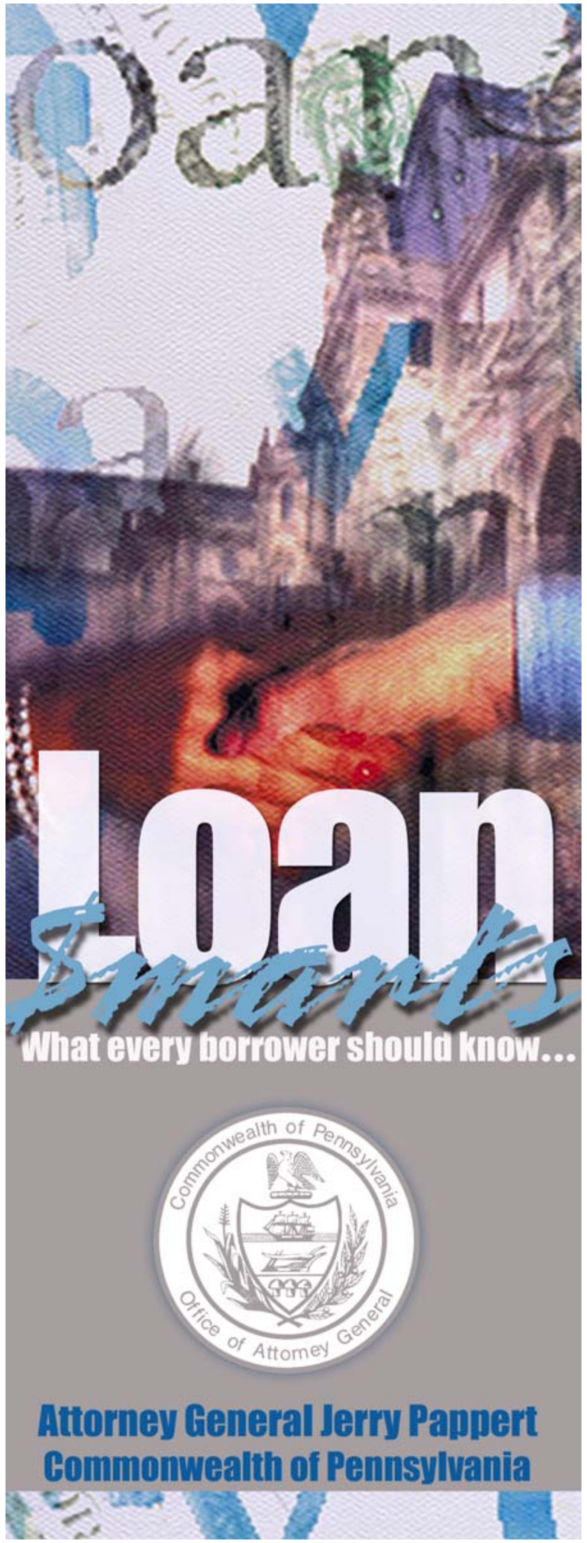
After closing, if you are having second thoughts, the Truth in Lending Act gives most borrowers at least three business days to cancel the deal. This "right of rescission" must be made in writing to the creditor. The lender then has 20 days to return any money you paid and must release any security interest in your home.

WHERE TO GO

If you think you have been taken advantage of by a lender or if you want more information on smart borrowing, contact the Bureau of Consumer Protection at 800-441-2555 (www.attorneygeneral.gov) or the Federal Trade Commission at 877-382-4357 (www.ftc.gov).

Pennsylvania
Office of Attorney General
Public Protection Division
Bureau of Consumer Protection

Pennsylvania Toll Free Hotline:
1-800-441-2555
www.attorneygeneral.gov



Dear Pennsylvanian:

Your home is likely your largest financial asset. That's why it is extremely important to know the facts when considering refinancing or borrowing against your home equity. While most lenders are legitimate and honest, there are unfortunately some unscrupulous ones that will try to take advantage of consumers. Some of those lenders make it sound as if tapping into your home equity is the answer to obtaining quick cash or paying off credit card bills. When interest rates are low, these options may appear especially attractive.

I want Pennsylvania consumers to be smart consumers. With this goal in mind, my Bureau of Consumer Protection and Public Education Unit have developed this brochure to help you become ***loan smart.***

Reading this brochure carefully will help you understand the different types of loans available to homeowners and help familiarize you with the issues associated with home lending. Choosing a loan can be confusing, and if you aren't sure about certain terms, you may agree to something you'll regret later.

Be certain to understand all the terms and conditions before agreeing to any loan, or you may put your most valuable asset at risk — ***your own home****.*

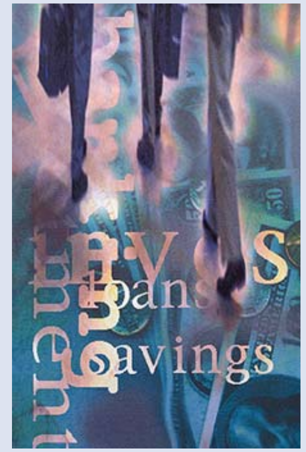
Gerald J. Pappert
Attorney General

Types of Loans

You may see advertisements for home equity loans, debt consolidation loans, second mortgages or offers to refinance your current loan. Understand that each of these loans use your home as collateral, which means you are putting that property in jeopardy if you cannot make the payments.

Home Equity Loans use a credit line to borrow against the value (equity) of your home. These loans provide you with large amounts of cash at relatively low interest rates, which may be tax deductible. Some loans have a final, balloon payment at the end of the term. You must either pay this lump sum or refinance the loan.

Refinancing means paying off an existing mortgage loan with the proceeds from a new loan, using the same property as collateral. It is important to note that you may be subject to the same costs you paid to get your original mortgage, including settlement costs, discount points and other fees. A prepayment penalty may apply for paying off the original loan early. The amount you save will vary depending upon factors such as interest rates, refinancing costs and tax consequences. Borrowers may have the option to refinance from an adjustable rate mortgage with a high interest rate subject to increases to a lower fixed-rate mortgage.



A Debt Consolidation Loan is a single loan, such as a home equity loan or the refinancing of an existing loan, used to pay off multiple debts - credit card bills, for example. Debt consolidation loans often offer a lower monthly payment, but with a longer term to pay off the loan. This means you may be paying more in interest in the long run.

A Second Mortgage is an additional mortgage on real estate that has already been pledged as collateral for an earlier mortgage. Second mortgages differ from first mortgages in several ways: they have a higher interest rate and are for a shorter term, usually 15 years or less. They may also require a balloon payment at the end of the loan.

UNDERSTAND ALL THE TERMS BEFORE AGREEING TO ANY LOAN!

Secured vs. Unsecured Loans

When you applied for a credit card, you did not have to put up your house, car or other property as collateral. You simply promised to pay your bills. Many people end up paying off credit card debt by borrowing against their homes, either by refinancing or through a debt consolidation loan or second mortgage. This may not be right for everyone. Defaulting on credit card payments will not result in the foreclosure of your home; however, missing payments on a second mortgage or home equity loan may.

Loan to Value Ratio (LTV)

The LTV is the percentage of the loan amount to the appraised value (or sales price) of your property. With a good credit history, most lenders will allow you to borrow up to 85% of the appraised value of your home, minus the amount you still owe on your first mortgage. You should never agree to a loan that is worth more than the value of your home.

Balloon Mortgages

A short-term, fixed rate mortgage with fixed monthly payments for a set number of years (usually 5-10) followed by a final payment of the principal is known as a balloon mortgage. Payments are usually lower because only the interest is paid each month. For example, borrowing $10,000 in a balloon mortgage means that a large payment is due in one lump sum at the end of the term. If you cannot make the final payment or refinance the amount, you can lose your home.

Mortgage Insurance

Lenders will often require borrowers who put less than 20 percent down on a home mortgage to purchase Private Mortgage Insurance (PMI). The insurance protects the lender in cases where the borrower defaults on the loan. Provisions of the federal Homeowners Protection Act, which took effect in 1999, establish rules for the automatic termination of PMI policies in certain instances, such as when the borrower's equity in the home reaches a certain level. Because this coverage can cost a borrower several hundred dollars each year, knowing when this insurance is no longer required can save you money.